21st Century Medicare: More Choices — Better Benefits

HEALTH SAVINGS ACCOUNTS (HSAs)

- The bipartisan agreement includes a provision establishing Health Savings Accounts or HSAs. HSA funds can be used to cover the health insurance deductible and any co-payments for medical services, prescriptions, or products. In addition, HSA funds can be used to purchase over-the-counter drugs and long-term care insurance, and to pay health insurance premiums during any period of unemployment.

- HSAs are similar to medical savings accounts (MSAs). However, MSA eligibility has been restricted to employees of small businesses and the self-employed. HSAs are open to everyone with a high deductible health insurance plan. The only limitation on the health plan is that the annual deductible must be at least $1,000 for individual coverage and at least $2,000 for family coverage.

- Contributions to the HSA by an employer are not included in the individual's taxable income. Contributions by an individual are tax deductible. Individuals, their employers, or both can contribute tax-deductible funds each year up to the amount of the policy's annual deductible, subject to a cap of $2,600 for individuals and $5,150 for families. Individuals aged 55-64 can make additional contributions.

- The interest and investment earnings generated by the account are also not taxable while in the HSA. Amounts distributed are not taxable as long as they are used to pay for qualified medical expenses, such as prescription and over-the-counter drugs and long-term care services as well as the purchase of continued health care coverage for the unemployed individual (via COBRA). Amounts distributed which are not used to pay for qualified medical expenses will be taxable, plus an additional 10% tax will be applied in order to prevent the use of the HSA for non-medical purposes.

- HSAs are portable, so an individual is not dependent on a particular employer to enjoy the advantages of having an HSA. Like an individual retirement account (IRA), the HSA is owned by the individual, not the employer. If the individual changes jobs, the HSA goes with the individual.

- In addition, individuals over age 55 can make extra contributions to their accounts and still enjoy the same tax advantages. In 2004, an additional $500 can be added to the HSA. By 2009, an additional $1,000 can be added to the HSA.